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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 355

HARTFORD STEAM BOILER INSPECTION AND INSURANCE COMPANY AND W. M. FRANCIS,
Appellants,

vs.

WILLIAM B. HARRISON, INSURANCE COMMISSIONER.

REPLY BRIEF FOR APPELLANTS.

HAROLD HIRSCH,
MARION SMITH,
Counsel for Appellants.

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The brief for the appellee introduces certain newly discovered reasons as to why the Georgia statute under attack bears (it is claimed) some real and substantial relation to matters within the domain of the police power. We file a reply brief mainly to reply to these newly discovered arguments. We note first, however, that there is no real difference between us as to the principles of constitutional law to be applied. Opposing counsel say:

> "We recognize the oft asserted principle that liberty of contract is one of the fundamental rights guaranteed by our Constitution, and that a State may not deprive a citizen of the United States of such privilege, or impair it, by the enactment of arbitrary or capricious law."

We claim no more than this.

Where the act in question bears a real and substantial relation to public health, morals, welfare, etc., then we concede that opposing counsel are entirely correct in saying that the legislative body is itself the exclusive judge of the wisdom of the legislation. But it must always be borne in mind that this relation of the statute to the public health, morals, or welfare must be real and substantial. A fanciful or imaginary relation is not sufficient. The means adopted must be reasonably suited to the ends sought. Wholly unnecessary restrictions cannot be applied. See cases cited and discussed in our original brief.

On page 9 of the brief opposing counsel suggest that the appellants must fail because they did not introduce proof on the constitutional questions. There is, however, no requirement that constitutional questions of this character must always be decided on proof. On the contrary, most of the rulings of this Court, holding statutes unconstitutional because of arbitrary and capricious interference with the fundamental liberty guaranteed by the Fourteenth Amendment, have been made on the basis of the provisions of the statutes themselves, togther with matters that are within the judicial cognizance of the Court. It is only in relatively recent years that cases have arisen involving complicated economic or sociological backgrounds where the introduction of proof has been found necessary. No such complicated factual background is here involved, or has been suggested at any point in the argument. Solely as illustrations of rulings invalidating statutes, without requiring the introduction of proof on the points involved, we refer to:

Liggett v. *Baldridge*, 278 U. S. 105;
Meyer v. *Nebraska*, 262 U. S. 390;
Quaker City Cab Co. v. *Pennsylvania*, 277 U. S. 389.

which are cited in our original brief to other points.

The number of such precedents could be multiplied but would serve no purpose.

Furthermore, where the statute involves a discrimination which appears arbitrary on its face the burden shifts to the side seeking to justify the discrimination to show some justification for its apparently arbitrary nature. For example, in the recent case of *Mayflower Farms* v. *Ten Eyck*, 297 U. S. 266, this Court said:

> "No reasons for the discrimination are disclosed by the record; and in the absence of such showing the Court has no right to conjure up possible situations which might justify the discrimination."

The crux of the brief of opposing counsel is found on pages 11, 12, 13, and 14, in which an entirely new basis of attempted justification is set out. That basis, briefly, is that agency costs should be related to the premium charged and should be kept uniform as a means of preventing rebating. *O'Gorman & Young* v. *Hartford Fire Insurance Co.*, 282 U. S. 251, is chiefly relied on in this connection. As heretofore pointed out, however, the ruling of the majority of this Court in the *O'Gorman* case was merely that excessive agency costs could be prohibited by statute as a means of keeping down insurance rates. What was said with regard to uniformity in its relation to rebating was in no sense a vital part of the decision, and if the question were actually involved in the present case we believe a strong argument could be made that the *O'Gorman* case is not authority for the position that uniform agency charges can be required as a means of preventing rebating where a State already has adequate statutes prohibiting such rebating. Georgia has such statutes. (Code § 56-218, § 56-9903).

However, the question is wholly beside the case at bar. This is, in no sense, a statute requiring uniform agency

costs. The whole argument as to the right of the State to require uniform agency costs is simply irrelevant where the statute involved does not attempt to make such a requirement, directly or indirectly. Under the Georgia statute insurance companies may pay their agents varying commissions for exactly the same services. If all agents are on a commission basis then the statute is complied with no matter how large the commissions or how much they vary for the same service. With reference to the argument of opposing counsel on this point their brief, on page 13, says: "It may be that this argument would seem more appropriate in support of legislative action fixing commissions." We agree.

On page 12, and more strongly on page 17, of the brief of opposing counsel, it is claimed that a salaried agent of an insurance company might also be licensed as a resident agent if paid on commissions for the business written as a resident agent. Just how this construction of the statute would save it is not apparent, but it plainly is an incorrect construction of the statute. The statute does provide, as opposing counsel say, that "the words 'resident agent' as used in this section are deemed to mean resident agents in the solicitation of such business from the public generally"; but the very next language in the statute is this: "and shall not include any salaried agent of any insurance company doing business in this State." The statute (p. 29, appendix to our brief) prohibits any fire or casualty company or company writing fidelity or surety bonds, from issuing any policy "except through a resident agent licensed by the insurance commissioner." Hence, no company can issue a policy except through a licensed resident agent, and no salaried employee can obtain a license as a resident agent; which necessarily reaches the result that no salaried employee can be qualified to write insurance at all. It is

not a question of how he is to be compensated for writing the insurance but is an absolute disqualification for being licensed for that purpose at all if he draws a salary.

Indeed, the present case could not have arisen at all except for this construction of the statute. The Insurance Commissioner did not refuse to issue the license because the Company did not expect to pay Francis commissions if he wrote business. No point with reference to this was raised. The Commissioner refused to issue the license because Francis, being a salaried employee, was disqualified from getting a license, and for that reason alone. The decision of the Supreme Court of Georgia necessarily recognizes the correctness of this construction of the statute.

But suppose the construction of opposing counsel were correct, it would mean about this: Assume that a branch manager, on a salary for his general services as branch manager, negotiated a certain contract of insurance; suppose he was entirely willing to do this as a part of his general work as branch manager. According to opposing counsel such branch manager could qualify as a resident agent and write the policy, provided the company paid him an extra commission for doing so, but could not qualify and write the policy unless he were given extra pay in the shape of a commission. The question then would be, whether the legislature could force the company by this statute to pay extra compensation through commissions to its salaried employee, so used, even though it and the employee were perfectly willing to contract that the service should be rendered under the general contract of employment covered by the salary. When so presented the case would fall within the principle settled by many decisions of this Court, that the legislature cannot require the payment to an adult individual, *suit juris*, and able to contract for himself, of more compensation than the amount for which he is willing to

contract with the company. *Adkins* v. *Children's Hospital*, 261 U. S. 525, and similar cases, are here in point. Indeed, the case is stronger against the constitutionality of such provision than the cases referred to, since here we are not concerned with any group suffering from economic handicaps, or with any problems connected with minimum pay for women, and the like.

And since opposing counsel are here asserting that the effect of the statute is to let insurance companies use their salaried agents, but to make them pay a commission also, then what becomes of the argument elsewhere made by opposing counsel that the purpose of the statute is to reduce agency costs? As we have heretofore pointed out, its actual operation is exactly the contrary.

On page 14 of the brief opposing counsel suggest that the statute can be sustained because insurance companies might pay unreasonable salaries which would run up agency costs. They might also pay unreasonably large commissions. There is really much more danger of commissions being unreasonably large than there is of salaries. But assuming that the legislature can prohibit unreasonably large salaries, it would nevertheless be true that the means of preventing unreasonably large salaries must be reasonable and properly adapted to that end. It is on its face unreasonable and arbitrary to prohibit any employment of any agent on any salary for the purpose of writing insurance merely because of a fear that some salary might be too large. The means adopted to correct such an evil, if there be one, from this standpoint, would be as unreasonable as to burn down a barn to get rid of a few rats.

It is also said, on page 14, that the answer avers that ninety-five per cent of insurance is written through commissioned agents or brokers, and that under the Georgia practice this specific averment of fact must be accepted.

We are entirely willing to accept it. The statute then would operate as to only the five per cent of insurance not written through ordinary brokers. It is quite obvious that this five per cent would be specially negotiated contracts covering special situations where the resident manager, or someone primarily salaried for other purposes, would act for the company. No one has ever supposed that the companies would specially employ agents on salaries whose sole business was to solicit insurance. Common knowledge of the business is to the contrary. Also, the actual insurance practice to this effect is set out in the appellee's answer (R. 9). The fact that the relevant insurance practices are set out in the appellee's answer is another reason why it was unnecessary for the appellants to introduce proof with regard thereto.

We have here, therefore, reached completely the point of actual operation of this statute. According to opposing counsel—and we accept the contention—about ninety-five per cent of insurance written would be wholly unaffected. The five per cent now ordinarily covered by policies issued by resident managers or other agents on salaries operating for other purposes, would be forcibly put over into brokers offices. The illustration given in our brief, therefore, of the operation of the statute becomes more important. This five per cent of the business, with which local insurance brokers normally have no connection, is business involving little or no agency costs to the companies. Their own salaried staffs handle it; no local broker is a producing cause of its being written. The statute, however, steps in and says that the companies are prohibited from letting their salaried representatives issue these policies even though the representatives are perfectly willing to issue them without asking any extra compensation, but as a part of their ordinary duties.

The Court will bear in mind that we have no complaint over the requirement in the statute that no one can issue such policies, whether salaried or commissioned, unless in every respect qualified in accordance with the strict requirements of the statute. Even though all of such requirements are met; even though the character, knowledge, and other tests are satisfactorily passed; exen though adequate records are kept; nevertheless, this statute prohibits any of such salaried representatives issuing policies. It forces the payment of unearned commissions on such policies to brokers who have had no connection with the transaction.

The final question in this case is whether this is a reasonable thing to do; whether it really serves anything connected with a public interest; or whether on the contrary it is merely a legislative fiat forcing the payment of unearned commissions. We believe the portion of the brief of opposing counsel to which we have referred helps us and the Court to get at the actual operation of the statute. We also believe that when we take a realistic look at what it actually does instead of conjuring up imaginary and fanciful reasons to justify it there is only one answer possible.

Counsel also say that in *LaTourette* v. *McMasters*, 248 U. S. 465, this Court said that an insurance broker was an agent for the insured as well as the insurer whose fidelity to both was a proper concern of the State. We have never denied that it is competent for the State to take reasonable means to provide that those writing insurance shall be men who will deal fairly with the insured. We do not believe the remark of the Court in the *LaTourette* case means any more than this. While that case dealt with a broker, not a salaried agent, and dealt with a statute which provided the broker should be the agent of the insured, whereas the Georgia statute says he is the agent of the insurer, nevertheless, we are willing to concede that the State can take

reasonable means to provide that only proper men, who will treat both parties fairly, may engage in writing insurance.

All of this is provided, however, in the statute, directly and adequately, as pointed out in our original brief, by requiring examination, license, etc. We have never felt that how the agent was paid had anything but a fanciful bearing on the subject, and have pursued the argument on that subject solely because counsel had made it. We have pointed out that if there was any substance to the argument it really meant that the State could by legislation undermine the loyalty of the agent to his company, although he was, under Georgia law, solely the agent of the company, and this, we said, and still say, is a shocking conclusion to reach. Apparently, however, opposing counsel have now reached the conclusion that the method of pay is not a material matter in order to secure fair treatment from an agent. On page 16 of their brief they say:

> "It can be no more said that requiring him to be compensated on a commission basis invites disloyalty to the company, than that to permit him to be compensated on a salary basis invites disloyalty to his customer."

We agree fully with this statement. The supposed connection is, and has always been, merely fanciful, but it leaves nothing of the argument of opposing counsel on this point.

On page 16 opposing counsel repeat the argument that an agent on a salary writing insurance policies is likely to be a mere clerk, who would not keep records, and say that the act does not require salaried agents to keep records. A correct statement is that the act does not require salaried agents to keep records unless they are licensed as resident agents. If they are licensed as resident agents they must keep records, and, inasmuch as they cannot write insurance at all

unless they are licensed as resident agents, it is clear that they are required by the terms of the statute to keep adequate records. It is also clear that a resident agent could not be a mere clerk unless the clerk had the knowledge, information, character, and experience necessary for him to pass the tests provided by law to qualify as a resident agent, in which event the fact that he was a mere clerk, if it were a fact, would be immaterial.

Having required the examination, and having required the keeping of adequate records, there is no possible justification for providing that no salaried agent should be licensed as a resident agent on the supposition that if the statute did not require these other things a salaried agent might not be satisfactory.

Where the legislative ends are fully accomplished by adequate and direct legislation a further restriction cannot be justified to accomplish the same ends.

See the discussion in *Weaver* v. *Palmer Bros. Co.*, 270 U. S. 402, commencing at the bottom of page 414.

Respectfully submitted,

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